

H-3107-1 - CONTINUATION, EXTENSION, OR RENEWAL OF LEASES

KeywordsII. Production on Federal Lands

This section of the Handbook contains procedural guidelines for leases and unit agreements and CA's that become producing, including the preparation of the first production memorandum, and guidelines for leases and CA's on which production has ceased.

EXTENSION BY
PRODUCTION

A. First Production

1. Production in Paying Quantities. The term "production in paying quantities" refers to actual lease production or the capability of lease production of oil or gas in sufficient value to exceed operation costs. In most Bureau offices, production figures of certain amounts (e.g., 75 thousand cubic feet (MCF) of natural gas or 10 barrels of oil daily) may be used to determine that a well is capable of producing in paying quantities without detailed analysis. Such standards are normally set locally based on historical economic experience for the location. Where such standards do not exist, or where the particular well location may make the application of such a standard inappropriate (e.g., a remote gas well many miles from any pipeline), or where the production tests show a potential daily production below the local standard, the AO must analyze the potential production to determine whether the well is capable of producing in paying quantities. Appropriate costs are to be deducted from the gross production income to determine profitability. Whether a well is capable of production is to be determined from the following guidelines:

PRODUCTION
IN PAYING
QUANTITIES

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KeywordsGUIDELINES FOR
DETERMINATION
OF PRODUCTION
IN PAYING
QUANTITIES

a. Costs to be included are Government royalty or minimum royalty; production payments or overriding royalties; administrative expenses, including reasonable overhead charges (not to exceed 10 percent of total operating costs); labor and repairs; certain taxes (such as State severance taxes, but excluding Federal income taxes); and other routine, ordinary costs of maintaining the lease, producing the wells, and marketing the products, such as expected ordinary expenses for workovers and equipment replacement. Minimum royalty and other annual holding costs may be applied in 12 equal parts on a monthly basis, and workover or similar expenses may be prorated over the time between such operations. The cost of capital equipment for the well operation, such as holding tanks and lateral pipelines, may be prorated over the expected well life, considering similar wells in the same vicinity. (See Kerr-McGee Oil Industries, Inc., et al., A-30481, 73 I.D. 110 (1966).) Note that paying well determinations under a unit agreement must also include the capability of the well to recover drilling and completion costs.

b. Costs to be excluded are drilling and completion costs of the well (except under a unit agreement); depreciation on equipment; and extraordinary expenses for pipeline construction, workovers, or equipment replacement resulting from unforeseen consequences such as fire or landslides.

c. For a lease to be continued by production, it must contain a well capable of producing oil and/or gas in paying quantities. This is a well that is actually in condition to produce in paying quantities. With oil wells, this normally includes all the equipment required to produce the oil from the well. Essentially, the well could produce by "throwing the switch on." The possibility that there is production in paying quantities behind the pipe for a zone that has not been completed and tested, or the possibility that further production could be obtained from the zone in which the well is completed, if that zone were treated or stimulated, are not in themselves sufficient reasons to consider the well capable of production in paying quantities. (See United Manufacturing Company et al., A-27608, 65 I.D. 106 at 111-115 (1958).)

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Keywords

d. A lease is producing in paying quantities if, under all relevant circumstances, a prudent operator would continue to operate a well for the purpose of making a profit and not merely to hold the lease for possible future use or for speculation. If the well operator begins producing the well immediately and sells the production to a refinery or a pipeline, the AO should infer that such production is in paying quantities. If the AO feels that the well is being produced solely to hold onto the lease for future use or speculation rather than to make money, a detailed analysis of the profitability is to be made before reporting the lease to be capable of production in a first production memorandum.

PRUDENT
OPERATOR
TEST

2. Date of First Production. The date a well is first capable of production in paying quantities is critical to rental or royalty obligations and is of extreme importance, in some cases, for determining whether a given lease remains valid. If the capability to produce in paying quantities occurs subsequent to lease expiration, the lessee may lose the lease and the hope for eventual profitable return from the investment in drilling the well, as discussed below.

DATE OF FIRST
PRODUCTION

The need to establish producibility prior to an expiration date becomes especially important whenever the lease involved is beyond its primary term and is not eligible for any further drilling extension. Two examples where the date of first production will be critical are: (1) the lease has previously been extended by drilling, but proved nonproductive at total depth, and the operator tries to complete the well at a shallower depth just before the end of the 2-year lease extension; and (2) a marginal well is completed in a producing unit on a lease that was eliminated from a unit by contraction and the operator must establish production before the end of the 2-year extension of the lease that resulted from the unit contraction.

FIRST PRODUCTION
FOR LEASES IN
EXTENDED TERM

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Keywords

In such cases, the leaseholder is responsible to be aware of the need to establish production or the capability of production in paying quantities prior to lease expiration. In these situations, where the lease is beyond its primary term and is not eligible for any further extension, a well must be capable of production in paying quantities on or before the day the lease would otherwise expire. Therefore, when the AO is aware that an operator is conducting operations shortly before such a lease would otherwise expire, close monitoring of the well is appropriate to ensure that operations do not occur after the lease expiration date until the AO has determined that the well was capable of production in paying quantities prior to the expiration.

The date the well is capable of production (whether or not the well is put on line immediately for actual production) is to be indicated as the date of well completion in the first production memorandum. That date is the date used by SO fluid lease adjudication and the MMS as the effective date for conversion of the lease from a terminable (nonproducing) status to a nonterminable (producing/royalty or minimum royalty) status. For natural gas, this will ordinarily be the date that the initial production test was run, assuming the gas flows from the well naturally. However, if additional equipment, such as a pumping unit, is required for the well to be physically capable to produce, the completion date will be the date such equipment is installed and is usable.

3. First Production Memorandum. The following guidelines apply to wells on Federal oil and gas leases or communitized and unitized areas that include Federal leases or lands.

FIRST
PRODUCTION
MEMORANDUM
PREPARATION

A first production memorandum (FPM) is used to identify the completion of the first well on a lease considered to be capable of production in paying quantities where the productive zone is already known to produce hydrocarbons in paying quantities in the area (see Illustration 8). A FPM is also required upon completion of the initial well under a unit agreement or CA involving Federal lands, even if previous first production memoranda have been written for any of the individual leases committed to the agreement. The FPM is the method used to transfer leases (in whole or in part) from terminable (nonproducing) status to nonterminable (producing/royalty or minimum royalty) status.

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The AO is responsible for monitoring new well completions or recompletions on Federal and Indian lands leases, and on unitized/communitized areas involving Federal lands. (See Sections X and XI of this Handbook for Indian lands leases.)

A FPM must be prepared promptly in all cases where Federal lands are directly involved, i.e., where the well is located on the Federal leasehold or on nonfederal lands communitized or unitized with Federal lands. Accordingly, the AO must monitor all new well completions and recompletions on Federal oil and gas leases and on nonfederal lands within all unitized or communitized areas that include Federal lands. The FPM is to contain the operator's name, well identification and location, pertinent geological data, the initial potential test data, and, if possible, a paying well determination. Within 10 days of receipt of the Well Completion or Recompletion Report and Log (Form 3160-4), prompt completion and transmittal of the FPM to the MMS-DMD is required (see Step II.A.3.e, below). The SO fluid lease adjudication also must receive a copy of the FPM to document the lease case file.

Entry of the appropriate action codes into Case Recordation also is required within 5 working days of completion of the FPM by the office that is delegated the responsibility within each BLM State. Appendix 3 provides the guidelines for entering all the production-related minimum mandatory action codes in ALMRS Case Recordation, e.g., DE 1775/2910 Action Code 643, PRODUCTION DETERMINATION; DE 1775 Action Code 644/DE 2910 Action Code 658, MEMO OF 1ST PROD-ACTUAL; DE 1775/2910 Action Code 650, HELD BY PROD-ACTUAL, etc.

a. Preliminary Determination of Paying Quantities. If the AO cannot initially determine from the initial potential test data and other available information that the well is capable of production in paying quantities, a comment to this effect is required in the "Remarks" section of the FPM. When this occurs, a supplemental report must follow within 120 days of receipt of sufficient information to determine the capability of the well. If oil is produced during testing of a well on a lease that is determined not to be capable of production in paying quantities, a notice must be sent to the MMS-DMD of the potential royalty obligation so that the MMS can set up a temporary account for such test oil or other products. In this situation, the lease account is not transferred to a minimum royalty status.

PRELIMINARY
DETERMINATION
OF PAYING
QUANTITIES

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Keywords

b. Reporting Initial Completion in Unit or Communitized Areas. A Federal oil and gas lease may be extended past its primary term by commitment to a federally approved unit or CA if a well is completed on a committed tract that is capable of producing unitized/communitized substances in paying quantities prior to the expiration date of the lease. Production in such quantities on any committed tract within the agreement area is considered to be on or for the benefit of each committed lease. Accordingly, a FPM (see Illustration 8) must be prepared promptly after the completion of the first unit or communitized well capable of producing unitized or communitized substances in paying quantities. Even if the first production in the unit does not qualify as a well capable of producing unitized substances in paying quantities, a FPM must be prepared if the well is or may be capable of production in paying quantities on a lease basis. This is required because the Interior Board of Land Appeals (IBLA) has concluded that a well capable of production in paying quantities on a lease basis, which is completed on a committed tract within a unit agreement will extend the term of all expiring Federal leases committed to the unit agreement for the term of the agreement and/or for so long as the well is capable of production in paying quantities. (See Yates Petroleum Corp. et al., 67 IBLA 246 (1982).) For the ALMRS Entry, see Appendix 3, page 32.

INITIAL
COMPLETION
IN UNIT OR
CA AREA

YATES DECISION

c. Reporting Subsequent Completions in Unit Areas. A FPM must be prepared for any subsequent unit well completion that establishes production in paying quantities for the first time on a lease within a unit area. The FPM will serve to set up a lease account for royalty purposes prior to establishment of a participating area (PA) and place the entire lease in minimum royalty status if the well is determined to be nonpaying on a unit basis, but capable of leasehold production in paying quantities. If a PA is established, the MMS would adjust the lease account so that only the acreage being allocated production would be in minimum royalty status.

SUBSEQUENT
COMPLETION
REPORT IN
UNIT AREA

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Keywords

d. Distribution of FPM. Copies of all FPM's are distributed within both FO and SO fluid mineral operations and to SO fluid lease adjudication. The FO/SO fluid mineral operations (as delegated the responsibility within each BLM State) also is responsible for notifying the MMS-DMD, as discussed below. Intra-FO operations (or intra-SO, where not delegated) notification of first production must include all affected organizational entities. If the well is located on a lease that is located in more than one BLM District, a copy of the FPM also must be sent to all other affected District Offices. Copies of the FPM's also are distributed to other BLM offices, as appropriate or as may be requested.

DISTRIBUTION
OF FIRST
PRODUCTION
MEMORANDUM

e. Coordination with MMS-DMD. At the time each lease or agreement (communitization or unitization) becomes productive, the FO/SO fluid mineral operations (as delegated the responsibility within each BLM State) must provide a copy of the FPM to the MMS-DMD (P.O. Box 5760, Mail Stop 3112). In accordance with the requirements of the BIA/BLM/MMS Memorandum of Understanding, receipt by the MMS-DMD must occur within 10 days of receipt of the Form 3160-4 by the FO/SO fluid mineral operations. The MMS-DMD also must be provided a copy of the approval letter for unit or communitization agreements upon approval of such agreements by the AO as notification of a new approval. In those instances where there is nonunitized production within the boundaries of an agreement, the MMS-DMD must be clearly advised of these circumstances. The MMS-DMD also must be advised of any circumstances where unitized lands are communitized with nonunit lands, i.e., with lands within the unit area but not committed to the unit plan, or with lands outside but adjacent to the unit area. Also, the MMS-DMD must be provided information concerning any overlapping or concurrent unit areas, communitized areas, and unit PA's.

TRANSMITTAL
OF FIRST
PRODUCTION
MEMORANDUM
TO MMS-DMD

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B. Adjudicative Processing (First Production - Federal Leases Only)

Responsible Official	Step	Action	Keywords
Field Office Operations	1.	Provide SO lease adjudication with FPM as soon as determination is made that the initial well on the lease, or in a communitized area or unit, is capable of producing in paying quantities.	PRODUCTION EVIDENCE
Unit Operations Supervisor	2.	Provide SO lease adjudication with approval of any unit PA, showing the the effective date of the PA, and whether it is the first initial unit PA. Approval of the first initial unit PA will cause the accounts of all the previously nonproducing leases committed to the unit to be transferred from terminable (nonproducing) status to nonterminable (producing/royalty or minimum royalty) status in the MMS-DMD system. Any subsequent PA that has an earlier effective date than the first initial PA is to be highlighted, to ensure that the automated records are updated/corrected and that the MMS-DMD is advised of the correct production date.	APPROVAL OF UNIT PARTICIPATING AREA
Adjudication	3.	Order appropriate case files from Docket. The FPM's for CA's must indicate what Federal leases are affected. For initial unit wells or initial PA's, this includes all committed unit leases. For subsequently approved PA's, only the case files of the leases with lands in the PA are required for processing.	
Docket	4.	Charge case files to Adjudication.	
Adjudication	5.	Review case file or abstract to determine whether the lease has ever been subject to segregation by partial assignment; if so, the leases embracing the segregated portions of the original lease are to be extended for 2 years from the date of discovery.	EXTENSION OF SEGREGATED PORTIONS OF LEASE

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Responsible Official	Step	Action	Keywords
	6.	Make sufficient copies of the FPM for processing the other leases for extension as indicated in Step V.A.2.b, below.	
	7.	Prepare notice to lessee of transfer of lease account from terminable (nonproducing) to nonterminable (producing) status in MMS-DMD, as appropriate (see Illustration 9).	NOTICE TO LESSEE
	8.	For unitized leases, the following guidelines apply:	
	8a.	If an initial PA has been approved, the accounts for all committed leases in the entire unit area are transferred from terminable (nonproducing) to nonterminable (producing) status.	
	8b.	If an initial unit well has been completed and determined to be producible but any PA determination is still pending, the account for the lease with the well, if Federal, is transferred from terminable (nonproducing) to nonterminable (producing) status. The accounts for all other leases paying rental will remain in terminable status, with the case files suspended to ensure the leases are not terminated pending a final determination.	
	9.	<u>OPTIONAL</u> : Stamp outside of case file "PRODUCING LEASE" to indicate that lease is held by actual or allocated production, or by location in a producing unit.	
ALMRS Entry	10.	Update ALMRS Case Recordation as follows, in accordance with the current data standards:	AUTOMATED NOTATION

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Responsible

Official	Step	Action	Keywords
		Enter Action Date (MANDATORY ACTION CODE): Date of production determination (date FPM was signed); DE 1775/2910 Action Code 643; Action Remarks: Numeric tie to appropriate action code listed below (see Appendix 3); and	
		Enter Action Date (MANDATORY ACTION CODE): Date of first production on lease (see Appendix 3); DE 1775/2910 Action Code 650; and	AUTOMATED NOTATION
	10c.	Enter Action Date (MANDATORY ACTION CODE): Date of first production (actual) on lease from FPM (see Appendix 3); DE 1775 Action Code 644/DE 2910 Action Code 658; Action Remarks: Numeric tie to Action Code 643, and enter well number and, if applicable, serial number of PA or CA; <u>OR</u>	
		Enter Action Date (MANDATORY ACTION CODE): Date of first production from off-lease well (see Appendix 3); DE 1775/2910 Action Code 651; and	AUTOMATED NOTATION
		Enter Action Date (MANDATORY ACTION CODE): Date of first production (allocated) from FPM rendering lease as in producing status (see Appendix 3); DE 1775 Action Code 645/DE 2910 Action Code 660; Action Remarks: Numeric tie with Action Code 643 and enter serial number of PA or CA; <u>OR</u>	
		Enter Action Date (MANDATORY ACTION CODE): Date lease is held by location in a producing unit (lease is committed to unit but does not have actual or allocated production - see Appendix 3); DE 1775/2910 Action Code 653; and	AUTOMATED NOTATION

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Responsible

Official	Step	Action	Keywords
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Enter Action Date (MANDATORY ACTION CODE): Date lease is held by location in a producing unit (see Appendix 3); DE 1775 Action Code 654/DE 2910 Action Code 659; Action Remarks: Numeric tie with Action Code 643 and enter unit serial number; and

Enter Action Date (MANDATORY ACTION CODE): Date lease account is transferred from terminable (nonproducing) to nonterminable (producing) status, i.e., date of first production stated in FPM); DE 1775 Action Code 057/DE 2910 Action Code 102.	AUTOMATED NOTATION
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Only one of the three DE 1775/2910 Action Codes 650, 651, or 653 is to be indicated on a lease at any given time to indicate the current, primary status of production.

Docket

11. File case file with active cases.

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KeywordsC. Cessation of Production

1. General. In order for any lease to be continued beyond its fixed term by production, it must be capable of producing oil and/or gas in paying quantities or be committed to a CA or unit agreement that is capable of production in paying quantities. Therefore, the AO is responsible for monitoring monthly production reports for this purpose. Close monitoring is especially important for leases passing out of a fixed term (at the end of either the original primary term or a definite extended term) into a status where the lease term continues only because of the lease's capability to produce oil and/or gas in paying quantities.

CESSATION OF
PRODUCTION

Equally important is close review of the status of leases that have been committed to producing oil and/or gas unit agreements for some time, but that are eliminated by a unit contraction and contain marginal wells. The capacity of such leases to produce, while not critical when the lease was located within the producing unit, becomes critical upon elimination from the unit. Extended delays in processing unit contractions, such as due to workload delays or extended suspensions of drilling or production requirements, causing the processing of a contraction long after its effective date, would justify close examination of all wells within a unit area prior to the elapse of a five-year period from the earliest effective date of any approved PA.

REVIEW STATUS
OF LEASES WITH
MARGINAL WELLS
WHEN LEASES
ARE CONTRACTED
OR ELIMINATED
FROM UNITS

Leases that cannot be profitably produced due to a temporary lack of market or unusually low prices for a period of time may occasionally be shut in or granted a suspension of production to ensure their future availability. The cessation of production envisioned by the following discussion is the situation when a lease would not be capable of producing regardless of the market/unusual price conditions that are occurring. For purposes of discussion, the word "lease" in this discussion also refers to unit agreements and CA's.

Lease production for communitized or unitized areas means production from the formation that is communitized or unitized.

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Keywords

2. When Production Has Ceased. Whenever production reports indicate that a lease that previously had been producing quantities of oil and/or gas has ceased to produce, the AO must determine whether the apparent cessation of production has been caused by the depletion of the reservoir, or whether the lease is still capable of production in paying quantities but is not producing for mechanical reasons, or is shut in for other reasons.

DETERMINATION
OF REASON
FOR CESSATION
OF PRODUCTION

a. Determination That Lease is Capable of Production. Unless the information available to the AO clearly indicates that the cause of nonproduction is the depletion of the producible reserves (which would be the case when production reports reveal a clear decline in production to a level where the potential revenue would not exceed the operating costs), the AO is to infer that the lease is still capable of production, but has been shut in for valid reasons by the operator. However, if the AO believes there is no valid reason for the lease to be shut in, the operator shall be ordered to place at least one well on the lease in a producing status within 60 days of receipt of such notification in accordance with 43 CFR 3107.2-3.

DETERMINATION
THAT LEASE IS
CAPABLE OF
PRODUCTION
IN PAYING
QUANTITIES

b. Determination That Lease is Not Capable of Production. If the AO concludes from the information available that the lease may not be capable of production in paying quantities, the operator shall be advised of this conclusion and given the opportunity to show that the lease is capable of producing in paying quantities or to commence reworking or drilling operations to restore production in paying quantities to the lease (see Illustrations 10, 11, and 12). (See Max Barash et al., 6 IBLA 179 (1972).)

DETERMINATION
THAT LEASE IS
NOT CAPABLE OF
PRODUCTION
IN PAYING
QUANTITIES

The lease shall not terminate, however, if the operator can demonstrate by well test or otherwise that the lease is physically and mechanically capable of producing leasehold substances in paying quantities. When an operator requires more than 60 days to run the necessary tests or to restore production in paying quantities from the zone that previously produced, upon request, if the operator presents justifiable reasons for the extended time, the AO may permit a longer time for "mechanical repair" and/or testing in the formation(s) from which production had been occurring.

REWORKING
OR DRILLING
OPERATIONS
TO RESTORE
PRODUCTION -
REQUEST FOR
EXTENSION
OF TIME

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Keywords

Operations to rework the well for production from another zone or the commencement of drilling operations on another well to restore production must be commenced within 60 days from the date of receipt of the letter (see Illustration 10, 11, or 12), absent an approved suspension of operations and/or production. To accomplish the demonstration or showing that the well is capable of production in paying quantities, the operator may be allowed mechanical repair work to reestablish or increase production for the well test. Although it is difficult to differentiate between "mechanical repair" and "reworking," the AO should allow any type of mechanical repair work necessary to physically reestablish or increase production from the existing productive interval during any extended period allowed for testing. Allowable mechanical repair work includes, but is not limited to, correction of any of the following: pump malfunctions, parted rods, casing leaks or collapse, and plugged screens or perforations.

REWORKING
OR DRILLING
OPERATIONS
FROM ANOTHER
ZONE OR WELL
TO RESTORE
PRODUCTION

In the absence of an acceptable showing that the lease is capable of producing in paying quantities or of reworking or drilling, the lease shall be considered terminated by operation of the law as of the date the operator receives the letter (Illustration 10, 11, or 12).

c. Unsuccessful Operations. If reworking or drilling operations are timely commenced within the 60-day period following cessation of production and are subsequently unsuccessful in restoring the lease to production in paying quantities, the lease shall terminate on the date that such operations ceased. If this date cannot be specifically determined, the AO shall assume that operations ceased on the last day of the month in which the last operations were conducted. If the operator takes no action in response to the 60-day letter, the date of last production is the date the operator received the letter.

UNSUCCESSFUL
OPERATIONS
TO BRING
WELL BACK INTO
PRODUCTION

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Keywords

d. Operator's Notice to Abandon. If, as a result of receipt of a 60-day letter from the AO, an operator files a Notice of Intent to Abandon (NIA) a well that is currently in a nonproducing status and is the last producible well, the date of last production is to be considered the date the operator received the letter. In approving the NIA, the AO is to remind the operator of any remaining time to commence reworking or drilling operations, pursuant to 43 CFR 3107.2-2. If such operations are performed and are unsuccessful in restoring the lease to production in paying quantities, the lease shall terminate on the date such operations cease. If the date cannot be determined, the AO is to assume that operations ceased on the last day of the month in which the last operations occurred.

OPERATOR'S
NOTICE TO
ABANDON -
WELL IN
NONPRODUCING
STATUS

However, if an operator files a NIA for the last producible well on a lease before the AO informs the operator of a determination that the lease is probably not capable of producing in paying quantities, the AO shall inform the operator by certified mail that the lease will terminate as of the date of receipt of such notification unless appropriate reworking or drilling operations are commenced within 60 days of receipt of the notification to restore production to the lease.

3. When Production Has Declined.

a. Review for Production in Paying Quantities. The FO operations personnel are to review all leases routinely, especially those in or entering an extended term due to production, so that such leases and agreements can be timely terminated as required. Illustration 13 describes the method to be used in determining whether a lease remains capable of production in paying quantities. In the absence of information to the contrary, whenever an operator produces a lease on a regular or sustained basis (at least 15 days every month except when shut in for mechanical or adverse weather conditions), the AO may assume that such lease is capable of production in paying quantities. If this is the case, a detailed economic analysis normally will not be required. However, when production from a lease in its extended term by production declines to a level that clearly appears to be nonpaying, the AO shall send the operator a certified letter similar in format to that shown in Illustration 14, 15, or 16.

DECLINE IN
PRODUCTION -
REVIEW FOR
PAYING
PRODUCTION

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Keywords

b. Unsuccessful Operations. If, within the 60-day period following receipt of the letter (Illustration 14, 15, or 16), the operator commences reworking or drilling operations timely on a lease that is continued solely by production, but those operations are not diligently pursued or the operator is unsuccessful in restoring the lease to production in paying quantities, the lease will terminate on the date that such operations ceased. If this date cannot be determined, the AO shall assume that the operations ceased on the last day of the month in which the last operations were conducted.

UNSUCCESSFUL
PRODUCTION
OPERATIONS
TO BRING WELL
BACK TO PAYING
QUANTITIES

c. Operator's Notice to Abandon. If, in response to the letter (Illustration 14, 15, or 16), an operator files a NIA to abandon the last producible well on the lease, the date of receipt of the letter by the operator is to be considered the date the lease was no longer capable of producing in paying quantities. The lease is to be considered terminated as of such date, unless reworking or drilling operations to restore production on the lease are timely commenced and diligently pursued (or unless the lease is extended as a result of the termination of an agreement).

OPERATOR'S
NOTICE TO
ABANDON LAST
PRODUCIBLE
WELL

When an operator files a NIA for a well that is currently producing and it is the last producible well on a Federal lease, and the operator has not received a letter in the format of Illustration 14, 15, or 16 for that well, the AO must inform the operator by certified mail that the lease shall terminate as of the date of receipt of such notification unless appropriate reworking or drilling operations are commenced within 60 days of receipt of the notification to restore production to the lease.

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Keywords4. When Well is Shut In.

a. Shut-in Well. For the purposes of this Handbook, a shut-in lease is defined as a lease with a nonproducing well that has been accepted by the AO as physically and mechanically capable of production in paying quantities, and is the only well or remaining well on the lease. Such a well may be shut in following its original completion (and the preparation of a FPM if it is the first completed producible well on the leasehold), such as when the well is located in an area remote from a marketing outlet. Or, a well may be shut in following a period of actual production in paying quantities of oil and/or gas, due to such factors as equipment failures, marketing rollbacks, or required balancing due to past overproduction. No lease shall be extended beyond its primary or fixed term by a shut-in well unless the AO is satisfied that the well remains capable of producing oil or gas in paying quantities based on a recent test of the well (see Illustration 13).

SHUT-IN
WELL

b. Annual Testing to Justify Continued Shut-in Status. Operators of leases in their extended term that are continued solely by reason of a shut-in well (or wells) shall be required to test at least one well on the lease every year to confirm that the lease remains capable of production in paying quantities. Further, each operator shall be required to submit data annually to show that construction of the necessary marketing facilities or marketing of the oil and/or gas is not economically feasible. At times, requiring annual one-point or four-point backpressure tests for gas wells with no pipeline connection could conflict with State orders against flaring. Under these circumstances, the AO may waive the annual test requirement where other available information indicates the well's producing capabilities. However, data must still be submitted annually to show that it is not economically feasible to construct the necessary marketing facilities. Any letter requiring the operator to perform the well test and/or to submit economic justification for continuing shut-in status shall advise that failure to perform the well test or provide sufficient economic justification will cause the BLM to assume that the lease is not capable of production in paying quantities (see Illustration 17). If the operator fails to perform the well test or does not provide economic justification, the AO shall send the operator a letter advising the operator of the 60-day reworking/drilling requirement (see 43 CFR 3107.2-2). (See Illustrations 10, 11, and 12.)

ANNUAL TESTING
TO JUSTIFY
CONTINUED
SHUT-IN STATUS

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Keywords

c. Negative Well Test. Where the well test fails to show that the lease contains a well that is capable of production in paying quantities (see Illustration 13), the AO shall send a certified letter to the operator providing notification of the AO's determination that the lease no longer contains a well capable of production in paying quantities. The letter shall advise the operator of the right to rework or drill within 60 days of receipt of such notification, and shall indicate that failure to perform such operations shall result in lease termination, effective the date of receipt of the letter. If reworking and drilling operations commenced within the 60-day period are unsuccessful in restoring the lease to production in paying quantities, the lease shall terminate on the date that such operations cease. If the specific date cannot be determined, the AO is to assume that operations ceased on the last day of the month in which the last operations were conducted.

NEGATIVE
WELL TEST

d. Placing Lease on Production. Where the lease contains a well that has been shown by well test to be capable of production in paying quantities, the operator may be required, as previously described, to submit data that justifies allowing the well to remain shut in. However, when the AO determines that the economics justify constructing appropriate sales facilities and there is no valid reason for the well being shut in, the AO will send the operator a 60-day notice by certified mail to commence the necessary actions to place the lease on production or provide BLM additional acceptable justification for not doing so. The subsequent decision letter to terminate the lease for failure to place the lease on production must contain a statement that the lessee has the right to appeal the decision.

PLACING LEASE
ON PRODUCTION

e. Operator's Notice to Abandon. If, in response to the letter (Illustration 17), an operator files a NIA to abandon the last shut-in producible well on the lease, the date of receipt of the letter is to be considered the date the lease was no longer capable of production in paying quantities. The lease is to be considered terminated as of that date, unless reworking or drilling operations to restore production to the lease are timely commenced and diligently pursued (or unless the lease is extended as a result of the termination of an agreement).

OPERATOR'S
NOTICE TO
ABANDON LAST
SHUT-IN
PRODUCIBLE
WELL

H-3107-1 - CONTINUATION, EXTENSION, OR RENEWAL OF LEASES

Keywords

When an operator files a NIA for a well that is currently shut in and it is the last producible well on a Federal lease, and the operator has not received a letter from the AO for that well requiring tests or justification for not placing the well back into production (Illustration 17), the AO must inform the operator by certified mail that the lease will terminate as of the date of receipt of such notification unless appropriate reworking or drilling operations are commenced within 60 days of receipt of the notification to restore production to the lease.

5. Preparation of Last Production Memorandum.

Whenever the procedures described above result in a determination that the well is no longer capable of production in paying quantities, and no other production occurs on or is allocated to the lease or CA, the AO shall timely prepare a Last Production Memorandum and forward it to the MMS-DMD (P.O. Box 5760, Mail Stop 3112) and to the SO fluid lease adjudication (see Illustration 18).

LAST
PRODUCTION
MEMORANDUM

H-3107-1 - CONTINUATION, EXTENSION, OR RENEWAL OF LEASES

D. Adjudicative Processing (Last Production/Cessation of Production - Federal Leases Only)

Responsible Official	Step	Action	Keywords
Adjudication	1.	Receive Last Production Memorandum from the FO operations staff.	EVIDENCE OF CESSATION OF PRODUCTION
	2.	If the lease is not otherwise extended, and is not within its primary or other extended term, prepare decision to the lessee, with the right of appeal, holding that lease is terminated. Advise in the decision that the bond is to remain in force and effect until all rents and royalties have been paid and final abandonment of all wells, including reclamation, has been approved (see Illustration 19).	LEASE TERMINATION DECISION
	3.	Suspend case file appropriately for 30-day appeal period.	
	4.	If the lease continues in force because it is still in its primary or an extended term, prepare an appropriate decision for the lessee (see Illustration 20).	
	5.	If the lease will be extended by termination of a CA or unit, or contraction from a unit, because of cessation of production, see Handbook 3105-1, Section IV.B, for processing.	
	6.	If the lease terminated, route case file for records update and competitive leasing following the appeal period.	
ALMRS Entry	7.	Update ALMRS Case Recordation using the current data standards:	AUTOMATED NOTATION
	7a.	Enter Action Date (MANDATORY ACTION CODE): Date of last actual production (see Appendix 3); DE 1775/2910 Action Code 646; Action Remarks: Numeric tie to Action Code 643, and enter well number and, if applicable, serial number of PA or CA; <u>OR</u>	

H-3107-1 - CONTINUATION, EXTENSION, OR RENEWAL OF LEASES

Responsible

Official Step Action

Keywords

NOTE: Remove DE 1775/2910 Action
Code 650.

- 7b. Enter Action Date (MANDATORY ACTION CODE): Date of last production allocated to lease (see Appendix 3); DE 1775/2910 Action Code 647; Action Remarks: Numeric tie to Action Code 643, and enter serial number of PA or CA; and

NOTE: Remove DE 1775/2910 Action
Code 651.

Enter Action Date (MANDATORY ACTION CODE): Date memorandum of last production was signed; DE 1775/2910 Action Code 643; Action Remarks: Numeric tie to appropriate action code in Step II.D.7a or 7b, above.

AUTOMATED
NOTATION

- 7d. Enter Action Date (MANDATORY ACTION CODE): Date lease production ceased/lease moves to minimum royalty status (when applicable; see Appendix 3); DE 1775/2910 Action Code 649; Action Remarks: Minimum royalty rate per acre; and

AUTOMATED
NOTATION

- 7e. Enter Action Date (MANDATORY ACTION CODE): Date lease expires; DE 1775/2910 Action Code 763; OR

Enter Action Date (MANDATORY ACTION CODE): Date lease terminated (based on date cited in last production memorandum); DE 1775 Action Code 790/DE 2910 Action Code 244; Action Remarks: Optional; OR

AUTOMATED
NOTATION

H-3107-1 - CONTINUATION, EXTENSION, OR RENEWAL OF LEASES

Responsible

Official	Step	Action	Keywords
	7g.	Enter Action Date (MANDATORY ACTION CODE): Effective date of lease extension (if lease is extended; see Handbook 3105-1); DE 1775 Action Code 258/DE 2910 Action Code 235; Action Remarks: THRU MM/DD/YY; and	AUTOMATED NOTATION
	7h.	Enter Action Date (MANDATORY ACTION CODE): Date extended lease expires; DE 1775/2910 Action Code 763; Action Remarks: Optional.	
	<p><u>NOTE:</u> Where cessation of production results in the termination (or contraction) of a CA or unit agreement, the leases committed to the (affected portion of the) agreement are entitled to a 2-year extension. Processing of such lease extensions and the cessation of production under such leases is discussed in Handbook 3105-1.</p>		